Joachim Nagel: Speech delivered at the change of office ceremony at the Regional Office in Saxony and Thuringia

Speech by Dr Joachim Nagel, President of the Deutsche Bundesbank, at the change of office ceremony at the Regional Office in Saxony and Thuringia, Leipzig, 10 June 2024.

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Check against delivery

1 Words of welcome

Ladies and gentlemen,

Welcome to this change of office ceremony at the Bundesbank's Regional Office in Saxony and Thuringia. It's wonderful to have so many of you in attendance. I take this as a sign of the high regard in which the work of the Bundesbank and, in particular, Hubert Temmeyer in the Free States of Saxony and Thuringia is held. I would particularly like to welcome Heike Taubert, Minister of Finance of the Free State of Thuringia, and Hartmut Vorjohann, Minister of Finance of the Free State of Saxony. Both of you will speak shortly; thank you very much for this!

I would also like to thank the young saxophone quartet of the Musikschule Leipzig, which kicked off this change of office ceremony in Leipzig, the "city of music". Some of those who are the same age as Mr Temmeyer or myself, upon hearing the melody, probably thought not only of Glenn Miller but also of Udo Lindenberg and his " Sonderzug nach Pankow" (literally, Special Train to Pankow). Irrespective of whether the roots lie in the east or in the west of Germany: with the four saxophones, we have just experienced one thing – namely that great things can come about when acting in concert. We have also experienced this in the European context.

It is true. United Europe was, first and foremost, a peace project. And still is. Over the past two years, this peace mission has gained a new significance that had hitherto no longer been thought possible. Yet a united Europe is also a booster of prosperity. There are now 31 countries that belong to the single European market. And indeed, these countries have, collectively, certainly seen far better growth than if they had gone it alone. This is a familiar observation to experts up and down the country. And this is something I point out time and again, for I believe that have to keep reminding ourselves of what a boon Europe is for us. For instance, since its creation in 1993, the single market has, in and of itself, increased economic output in the EU by around 3 to 5½%.[1] This is suggested by studies. By contrast, the United Kingdom's exit from the EU, also known as Brexit, has so far reduced UK economic output by 6%, according to a UK study presented this year.[2]

In my view, the advantages of a united Europe could have become even clearer in the run-up to the European elections. Fortunately, a group of firms has highlighted the importance of European integration for prosperity, growth and jobs and has sent a signal for diversity, openness and tolerance. And I, too, always advocate for this view.

Now it is a matter of upholding the banner of Europe and continuing to champion European cooperation.

2 Dr Hubert Temmeyer

From openness and the benefits of international cooperation to you, my dear Mr Temmeyer. And this is just a small step: for thinking in terms of international contexts – and shaping those contexts – has played a major role in your career. You're essentially a textbook example of working in an international setting. But let me start from the beginning.

A native of Osnabrück, you studied economics in Siegen and then moved on to the far north to do research work at the University of Kiel and obtain your doctorate. After a little over two years at the Federal Economics Ministry, you joined the Bundesbank nearly 33 years ago, namely in the department then known as "International Relations". You were to work on their issues for the next 25 years, of which a total of 17 years were spent at our headquarters in Frankfurt. Your last post there was Deputy Head of the International Monetary Affairs Division. You spent three years in Paris on secondment to the OECD;

Beginning in 2011, you spent five probably particularly prominent years of your career in Washington DC working at the International Monetary Fund (IMF) as the Executive Director for Germany. There, but also in Frankfurt before that, you were very busy with the IMF's major quota and governance reform, which was adopted in December 2010 by the IMF's governing bodies, i.e. shortly before you became Executive Director. However, it did not enter into force until the beginning of 2016. That is how long it took for the requisite majority of nations, including the United States, to ratify the amendment to the IMF Articles of Agreement and their own quotas. It was a tough struggle, which should not surprise anyone – after all, global influence was at stake. We are also noticing something similar at present. And not only in the debate on IMF governance. Another major topic during your tenure at the IMF was the euro area sovereign debt crisis. During the acute part of the crisis, the aim was to avert the worst. This is where the IMF made an important contribution. And you brought to the table your sizeable economic expertise and your particular skill in in navigating talks with discretion. You injected the Bundesbank's views and were an effective proponent of stability.

As an advocate for stability and a seasoned economist, you were also held in high regard and were in high demand here in Saxony and Thuringia. You were President of the Bundesbank's Regional Office and represented the Bundesbank in the region for eight years. One of your main concerns was to impart knowledge of central bank issues, which are often not exactly simple, and thus to convey an understanding of current developments. You considered the "Forum Bundesbank" series and the banking evenings to be formats that lent themselves particularly well to exchanging ideas with the general public and experts from the business and financial world. A total of 90 of these events took place during your tenure, with presentations by our skilled Bundesbank staff in Leipzig, Dresden, Erfurt and Chemnitz. You chaired the debates in an expert manner and to the benefit of all. And, from time to time, you yourself were the knowledgeable speaker. These offerings were, and are, very popular and well attended.

The topic of the "digital euro" has encountered particularly keen interest. I am personally pleased about that. This is because the "digital euro" project will be *the* central strategic project of the Bundesbank and the Eurosystem in the coming years. The digital euro would deliver a host of benefits to the public. Let me just list three of them here. It would be a European digital means of payment that could be used throughout the euro area. It would provide payers with greater privacy protection than we have seen with other digital means of payment thus far – a point which is all the more important given that the protection of privacy is a key concern voiced by people in surveys on the digital euro. And it would make digital payments in the euro area independent of foreign payment service providers. At your events, dear Mr Temmeyer, you have also repeatedly emphasised that the digital euro should complement cash in an appropriate and useful manner and not replace it.

In accordance with its statutory mandate, the Bundesbank will continue to ensure that a reliable and sufficient supply of cash is available at all times and anywhere. With our branch network, we have put in place important framework conditions for our business partners, such as credit institutions, retailers and CIT companies. However, we must also take into account the decline in the use of cash by the public in recent years. The Bundesbank is currently preparing a future-proof branch strategy that will ensure resilience to crises. At the same time, economic efficiency and sustainability are set to be improved. Communicating the new branch strategy will be an important task for the Regional Office Presidents.

You, dear Mr Temmeyer, have always set great store in exchanging ideas with colleagues. You did not take lightly any topic that was of particular concern to your colleagues. You always lent a listening ear – whilst on and off duty alike. For example, at the Leipzig company fun run, which you took part in eagerly and in impressively good shape. You have always addressed the issues that were occupying the staff at your Regional Office and branches. I know that you are highly respected for this.

3 Economic activity, inflation and monetary policy

Ladies and gentlemen,

When the Bundesbank President pays a visit, you would certainly also expect him to talk about the economic situation. I'm happy to oblige. The German economy expanded by 0.2% in the first quarter after contracting in the fourth quarter of 2023. Construction saw notable growth in the first quarter of 2024, as did industry and services. But there were still no signs of a broad-based, sustainable recovery in industry. Demand at home and abroad has remained feeble so far, and the uptick in construction activity is probably mainly the result of the favourable weather conditions. Increased financing costs and elevated uncertainty are putting a damper on investment. And consumers have been keeping their purse strings fairly tight so far, judging by the first-quarter dip in private consumption. There have been some encouraging signals as well, though. Lower inflation rates and strong wage growth, combined with what remains a robust labour market, could spur an upswing in household consumption. And enterprises' business expectations have brightened significantly of late. On aggregate, economic activity is likely to gradually pick up some momentum. We are expecting to see slight growth of 0.3% for 2024.

The euro area economy is faring better than Germany's, but the same influences are at play. Hence, Eurosystem staff are expecting private consumption to also be the main factor driving the recovery in the euro area. Like in Germany, the euro area labour market is proving to be remarkably robust, with euro area unemployment at an all-time low.

For all this, what matters from a monetary policy perspective is that the persistently too-high inflation returns to its 2% target. The flash estimate put euro area inflation in May at 2.6%. That is up somewhat on April, but significantly down on the fourth quarter of 2022, when euro area inflation was still running at around 11%. But inflation isn't going to converge towards its 2% target of its own accord. Month-on-month services inflation in May stood at 4.1%, according to the flash estimate. Above-average wage rises were a notable factor here. The trade unions take the view that these wage hikes are recouping some of the losses in real wages suffered over the past three years.

The Eurosystem staff macroeconomic projections published last week see headline euro area inflation standing at 2.5% this year, which is an upward revision of 0.2 percentage point compared with the March projections. Headline inflation is, however, expected to decline further towards our 2% target and reach that level towards the end of 2025, according to the current projections.

Given the big picture, which I have only briefly outlined here, the Governing Council of the ECB lowered the key ECB interest rates last Thursday. This move comes after ten consecutive interest rate hikes, the first of which was in July 2022. Rates were then left at the high level they had reached as of September 2023, being held there for nine months. And now the Governing Council has lowered the interest rate on the deposit facility, which is currently the main rate for the monetary policy stance, from 4% to 3.75%. And what does the road ahead look like for the key ECB interest rates? One thing is beyond dispute for me: we need to remain cautious. You see, future economic and price developments are still fraught with uncertainty. To use a metaphor, I wouldn't say we're at the summit of a mountain from which the only way is down. Rather, it's better to say we're on a crest where we still need to find the right point for the further descent. Following this line of thinking, the Governing Council emphasised again last week that decisions will continue to follow a data-dependent and meeting-by-meeting approach.

4 Business dynamism and productivity

Ladies and gentlemen, over the past two years the high inflation featured strongly in the question of how to assess Germany's economic situation. Now it is the medium to longer-term outlook that is generally shaping the debates again. Some say a "jolt" is needed because, they argue, improving the framework conditions for the German economy is the key to safeguarding our prosperity. The current bout of weakness is worrying many people, and that's mainly because our country, the German economy, is facing major longer-term challenges. The first two challenges I would mention are the need to decarbonise the economy and the ageing of our society. Both of these will involve considerable burdens. Plus there are geopolitical tensions, which are difficult to predict but undoubtedly a major source of risk.

All the more important, then, to have solid growth. That would have to be achieved, in particular, through strong productivity growth. You see, demographic change is already creating labour market impasses right now, and these are also dragging on economic output. However, productivity growth has been in decline for several years now, and not just in Germany. Only recently did we once again highlight the various factors at play here in our Monthly Report. Our experts wrote that digital sectors have contributed significantly less to productivity growth in recent years than they did at the beginning of the century.[3] Digital upskilling and more investment in digitalisation across the entire value chain could help give productivity in Germany a significant boost. Another reason for the shrinking productivity growth is fading business dynamism,[4] as measured by the number of firms that enter and exit the market.

Germany has seen both firm entry and firm exit numbers decline sharply over the past two decades. At first glance, a drop in the number of businesses exiting the market sounds like good news – after all, business closures often take their toll on the people involved. However, stronger business dynamism benefits the economy as a whole. It tends to be conducive to productivity growth and thus to expansion over the long run. There's no need to explain why that's a good thing as far as firm entries are concerned. After all, start-ups are an important building block for economic growth: they nurture fresh ideas and bring them to market maturity. You can get a particularly good sense of this here in Leipzig, with its start-up scene.[5]

At the same time, innovative newcomers crowd less-profitable firms out of the market. But that has its upsides, too. You see, the people who worked at those firms switch to enterprises with a brighter future. And capital, too, can also flow into more-profitable firms. This is a process that Austrian economist Joseph Schumpeter called "creative destruction". It is a process that unleashes productivity growth, boosts prosperity, and even leads to greater economic security in the long term.

In Germany, market entries and exits in 2023 were down by almost one-third – specifically, 30% – compared with 2004. This sharp decline partly explains why productivity growth is weak and receding in Germany. There is another point that backs up this view. These years did not only see a drop in the number of market entries and exits – they also saw a divergence of productivity levels between firms within a given market. In other words, firms trailed ever further behind sector leaders in terms of their productivity. From an economic perspective, this suggests that "declining allocation efficiency" was at play – that is to say, the allocation of production factors trailed increasingly behind levels that would have been needed to achieve optimum productivity. Yet the reallocation of labour and capital away from inefficient firms to more efficient ones ranks as a key driver of productivity growth in the economy at large.

If we now explore what is behind the decline in market entries, the general ups and downs of economic activity are one factor. Firms tend to be established in upturns, while more are closed during downturns. In addition, rising uncertainty can dampen the firm entry rate on a lasting basis. Indeed, the market entry rate in Germany and the euro area has been conspicuously weak ever since the financial, economic and subsequent sovereign debt crisis. Besides these cyclical factors, though, there are also structural constraints. In particular, demographic ageing acts as a drag on business dynamism. A study on the federal state of Saxony as a start-up location, for example, found that when start-ups were established, 59% of the people who set them up were aged between 25 and 34 – that is to say, they were young.[6]

This makes it all the more important for us to support business dynamism wherever possible. Besides cutting excessive red tape, improving access to funding sources is another item I would mention here. As you probably know, I am particularly keen to press ahead with the capital markets union in Europe. The further we make progress on these fronts, the sooner the challenges I have just mentioned will be able to emerge as opportunities – opportunities to boost innovation, economic momentum, future-proof jobs and stronger growth.

5 Concluding remarks

That concludes my outlook, and I would now also like to conclude my speech by turning back to you, Mr Temmeyer. You are leaving the Bundesbank at the end of July, but thanks to some untaken holiday entitlement, you will be clearing your desk sooner. You have served the Deutsche Bundesbank and the stability of the financial system for a long time – for 33 years, in fact – and done so expertly, conscientiously and not just that: with exceptional dedication and success. On behalf of the Executive Board, please accept my heartfelt gratitude. It will probably take a little time to switch from such a hands-on professional career to life as a pensioner. I trust that memories of highlights from your professional life will be among your "favourite things", to quote from the piece of music you have chosen to round off today's event.

You are handing over to the incoming President, Guido Müller, a Regional Office in Saxony and Thuringia that is in the best of shape. Mr Müller has already learned the ropes here, and I expect many of you will have already got to know him. He will seamlessly take over Mr Temmeyer's work. Guido Müller previously served as Director General Construction Management in Frankfurt. A change is also in the offing regarding the position of Head of Internal Operations, which simultaneously involves deputising for the President of the Regional Office. Effective February 2025, Susann Schwer will succeed Bernhard Häffner, who will then be retiring from the Bundesbank. Ms Schwer currently heads the Regional Division Banking and Financial Supervision for Saxony and Thuringia. Dear Mr Müller, I wish you good fortune and every success in your new task here in Saxony and Thuringia.

And now I take pleasure in presenting you, Mr Temmeyer, with your retirement certificate and you, Mr Müller, with the letter awarding you the position of new President of the Regional Office – and, as an expression of my gratitude, a bouquet for each of you.

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[1] Felbermayr, G., J. Gröschl and I. Heiland (2022), Complex Europe: Quantifying the cost of disintegration, Journal of International Economics, Vol. 138, September 2022 and Mayer, T., V. Vicard and S. Zignago (2019), The cost of non-Europe, revisited, Economic Policy, Vol. 34, April 2019. A study conducted on behalf of the European Commission estimates that EU GDP is as much as 8 to 9% higher thanks to the single market; see in 't Veld, J. (2019), Quantifying the Economic Effects of the Single Market in a Structural Macromodel, European Commission, Discussion Paper 094, February 2019.

[2] Cambridge Econometrics (2024), London's economy after Brexit: Impact and implications.

[3] Deutsche Bundesbank (2023), The impact of digitalisation on labour productivity growth, Monthly Report, March 2023.

[4] Deutsche Bundesbank (2024), Dynamism in the German corporate sector down overall in last two decades, Monthly Report, March 2024.

[5] See Studie zum Gründungsstandort Sachsen (2022), pp. 76 f.

[6] See Studie zum Gründungsstandort Sachsen (2022), pp. 48 f.